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SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1931

No. 401

AMERICAN SURETY COMPANY OF NEW YORK,
PETITIONER,

vs.

THE GREEK CATHOLIC UNION.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT AND BRIEF IN SUPPORT THEREOF.

JAMES M. MAGEE,
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EDMUND W. ARTHUR,
Of Counsel.

(36,215)

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PETITION FOR WRIT OF CERTIORARI.

To the Honorable the Justices of said Court:

The petition of American Surety Company of New York respectfully sets forth:

Summary Statement of the Matter Involved.

THE QUESTIONS PRESENTED.

1. Whether a surety for compensation upon a treasurer's bond covering *inter alia* his selection of depository is liable as an insurer for subsequent loss of interest on a deposit sustained by the obligee where, after

breach of bond, said obligee, in an effort to minimize an anticipated probable loss through failure of depository, entered into an agreement with a new depository to waive interest on its deposit for four years as an inducement to the new depository to take over the business of the former one and avert its failure, said agreement having been entered into without notice to the surety and involving the consequent destruction of the surety's right of subrogation and of the possibility of proving the variance in the risk prejudicial.

2. Whether in such case the loss sustained was due to cause beyond the scope of the bond.

THE ESSENTIAL FACTS.

This action arose by suit in assumpsit against George Kondor, principal, and American Surety Company of New York, surety upon his bond as treasurer of The Greek Catholic Union, a beneficial society organized under the laws of the Commonwealth of Pennsylvania.

The bond guaranteed the fidelity of Kondor, bound the obligors to pay loss due *inter alia* (*a*) to failure of principal to perform his duties as prescribed by the constitution and by-laws of the order, (*b*) to failure to keep intact and account for funds in accordance with the constitution and by-laws, and (*c*) failure of depository.

It was alleged, and by jury found that Kondor had breached his bond, the specific charge being that he had carried on deposit at Johnstown, Pennsylvania,

in a bank of which he was treasurer, an aggregate amount in excess of the limit allowed by the by-laws and excessive in proportion to the assets of the depository bank.

This bank came into financial difficulties. Upon an examination by the banking department of the State of Pennsylvania, its officers were notified on a Friday or Saturday that unless indicated steps were taken to correct its condition it would not be permitted to open on the following Monday. The officers of various banks in the city conferred with a view to averting failure of the depository. Finally, as an inducement to a trust company to take over and conduct the business of the depository bank, The Greek Catholic Union, obligee of the bond in suit, agreed in writing to allow two hundred thousand ($200,000.00) dollars to remain on deposit with the trust company for a period of four years without interest unless within that period there was realized from the assets of the depository an amount sufficient to pay all its depository liability. This agreement was made without knowledge or consent of the surety and following it the business of the depository was transferred to and continued by the trust company without interruption and without the payment of interest to the fraternal society.

The alleged loss which the jury was permitted to consider and for which the verdict was rendered was the amount of interest on this deposit of two hundred thousand ($200,000.00) dollars figured at five and two-tenths (5.2) per centum, with interest thereon from date of claim.

Judgment on the pleadings was entered in favor of the American Surety Company of New York, the surety, by the District Court in accordance with practice under the law of Pennsylvania (R. 7). This was reversed by the Circuit Court of Appeals (R. 2) in an opinion by Buffington, J., in which Davis, J., concurred, Woolley, J., filing a dissenting opinion, 25 Fed. (2d) 31. The case being remanded for further proceedings, on the first trial the jury disagreed (R. 3), on second trial a verdict was rendered in favor of the plaintiff for forty-six thousand eight hundred ($46,800.00) dollars (R. 3), from judgment on which entered against both defendants an appeal was taken.

On argument, the Circuit Court of Appeals affirmed the judgment of the District Court. Petitioner now seeks a review of that affirmance as to the surety.

Reasons Relied on for the Allowance of the Writ.

The rulings of the court below if allowed to stand will

(*a*) Largely unsettle the law of suretyship by introduction of a radical relaxation of a well established rule.

(*b*) Add an additional burden uncontemplated and uncompensated to millions of dollars of outstanding fidelity insurance written upon the basis of pre-existing law; and

(*c*) Add confusion to the law of suretyship by permitting, without consent of a surety, the

addition of new speculative risks which cannot be specified in advance or anticipated, resulting in general unsettlement of the schedules of rates of all commercial companies, to the discouragement of a business the sphere of which is rapidly increasing in importance.

WHEREFORE your petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the Circuit Court of Appeals for the Third Circuit, commanding that court to certify and to send to this Court for its review and determination, on a day certain to be therein named, a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket No. 4537, AMERICAN SURETY COMPANY OF NEW YORK and GEORGE KONDOR, appellants, *vs.* THE GREEK CATHOLIC UNION, appellee, and that the said judgment of the Circuit Court of Appeals may be reversed by this Honorable Court, and that your petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

And your petitioner will ever pray.

AMERICAN SURETY COMPANY OF NEW YORK,
By JAMES M. MAGEE,
Counsel for Petitioner.

EDMUND W. ARTHUR,
Of Counsel.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1931

No. 401

AMERICAN SURETY COMPANY OF NEW YORK

vs.

THE GREEK CATHOLIC UNION.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Opinion of the Court Below.

The opinion of the Circuit Court of Appeals when the case was before it on judgment on the pleadings was written by Buffington, Circ. J., Davis, Circ. J., concurring. Woolley, Circ. J., wrote a dissenting opinion. These are reported in 25 Fed. (2d) 31.

The opinion of the same court in the second appeal, adopting without restating the statement of law made in the former opinion, was written by Buffington, Circ. J., Thomson and Thompson, Circ. JJ., concurring, and was filed August 14, 1931 (R. 307).

Jurisdiction.

(*a*) It is believed that the jurisdiction upon writ herein prayed for is sustained by Section 240 of the Judicial Code as amended by Act of February 13, 1925, c. 229, Sec. 1, 43 Stat. 938 (U. S. Code, p. 906, sec. 347).

(*b*) The date of the judgment to be reviewed is August 14, 1931 (R. 310).

Statement of the Case.

A full statement of the case appears in the petition. In the interest of brevity it is referred to without repeating at this point.

Reference, however, is made for emphasis to the facts—

(*a*) That a variance of the risk was accomplished by the obligee without the knowledge or consent of the surety;

(*b*) That obligee substituted a fixed certain loss for an uncertain probable loss;

(*c*) That by the action of the obligee the surety was deprived of its right of subrogation, its opportunity for salvage, and the possibility of proving the variance prejudicial.

Specification of Assigned Errors.

1. The Circuit Court of Appeals erred in refusing to find and hold that under all the evidence the verdict should have been for the surety defendant.

2. The Circuit Court of Appeals erred in refusing to find and hold that the material variance of the risk insured by appellant, whereby a new hazard not covered by the bond was sought to be imposed upon appellant and it was deprived of opportunity both for subrogation and for obtaining proof that the variance was prejudicial, constituted a full defense to the claim against the surety.

That is to say:

3. The Circuit Court of Appeals erred in refusing to sustain appellant's 3rd (R. 300), 5th (R. 301), and 8th (R. 302) assignments of error.

The opinion (R. 309) concludes—"We are of opinion no error is shown and the judgment below is affirmed."

ARGUMENT.

Summary.

A. Importance of the business affected.

B. The decision of the Circuit Court of Appeals, if allowed to stand, will unsettle the law of suretyship by introducing a new and radical relaxation of the rule of *strictissimi juris* as applied to surety for compensation.

(1) By permitting material variance or substitution of new risk without consent of the surety.

(2) By making surety liable without its consent for loss due to cause beyond the scope of the bond.

(3) By throwing upon a surety defending on the ground of material variance of the risk by the obligee the burden of proving the variance prejudicial, though the action of the obligee has destroyed all possibility of such proof.

C. Reference to authorities.

Point A.

The requirements of modern business for fidelity and similar suretyship have exceeded for many years the possibility of being met by individual sureties. Business, law and the social organization in general demand a form of insurance which is being supplied ever in greater measure by a large number of commercial surety companies. There is today outstanding millions of dollars of fidelity insurance written in contemplation of the legal requirements and interpretation heretofore current. It is common knowledge that the rates charged by way of premium have been calculated in an amount necessary to set up a legal reserve against the hazard and compensation for the service.

Point B—General.

The questions presented by this case are, we believe, new to the body of surety law. They arise and find their large importance in the evolution of this law to fit the case of the compensated surety. The rule of *strictissimi juris* as applied to the individual surety has been gradually and increasingly relaxed in the case of surety for compensation. The ruling in the

instant case carries this relaxation beyond a danger point, in that it adds an additional hazard uncontemplated when the insurance was written and constitutes a burden against which the insurers are not secured and for the assumption of which they are not compensated. Its affirmance must be highly injurious to many and possibly disastrous to some surety companies through inability to cover the increased hazard on outstanding insurance. It must be, in a measure, subversive of the usefulness of the compensated surety generally through increase of expense to patrons, disturbance of schedules and uncertainty of risk, the cost of insuring which can be actuarily ascertained, if at all, only after long years of experience.

Point B (1) and (2).

By the terms of its bond petitioner assured The Greek Catholic Union against loss through misconduct of the treasurer, or failure to perform the duties prescribed, or through failure of the depository.

Assuming the bond to have been breached by the misconduct and default of the principal, the Union, to avert an anticipated probable loss through threatened failure of the depository, entered into an agreement to accept a fixed certain loss as an inducement to another bank to take over the depository. Here was a material variance in the contract: The substitution of a new risk without consent of the surety, followed by an effort to hold the surety liable for the loss sustained by the Union through its own act, a cause beyond the scope of the bond.

Point B (3).

The merger of the failing depository and the continuance without interruption of its business in the hands of the merging bank deprived the surety of any right of subrogation, of any salvage through participation in the distribution of assets, and of any possibility of ever proving that by other management loss might have been averted. To hold that in such case the surety must prove that it was prejudiced by the voluntary act of the obligee seeking its own advantage is to tear down the security of a definite contract and to impose upon the surety a task beyond the power of even a modern Hercules to perform, that is, "to prove the consequences of a thing that never happened."

Counsel for petitioner respectfully refer to the dissenting opinion of His Honor, Judge Woolley, when this case was first before the Circuit Court of Appeals as expressing in concise, vigorous and cogent language the position of your petitioner, *then* upon the facts disclosed by the readings, and *now* upon the facts disclosed by the evidence (see 25 Fed. (2d) 31).

Point C.

That the decisions of your Honorable Court have never contemplated such a radical and disturbing innovation in the law of suretyship may be indicated by the language of the following decisions:

Guarantee Company of N. A. vs. Mechanics' Savings B. & T. Co., 183 U. S. 402 (1902), Fuller, C. J.

There the court, in commenting on the decision in *American Surety Company vs. Pauly*, 170 U. S. 133,

on the subject of fidelity insurance and the rule of construction of a policy in favor of the insured, remarks (opinion p. 419):

> "But this rule cannot be availed of to refine away terms of a contract expressed with sufficient clearness to convey the plain meaning of the parties, and embodying requirements compliance with which is made the condition to liability thereon."
>
> *United States Fidelity & Guaranty Co. vs. Pressed Brick Co.*, 191 U. S. 416 (1903).

Mr. Justice Brown in discussing in the opinion of the court the application to surety bonds of the rule of *strictissimi juris* and its relaxation in the case of the compensated surety used the following language: (P. 426

> "The facts of this case do not call for an expression of opinion as to whether, if an unusual credit were given, and in the meantime the principal obligor had become insolvent, or the surety were otherwise damnified by the delay, it might not be exonerated, since neither of these contingencies supervened in this case, and we are remitted to the naked proposition whether the giving of a customary credit, with no evidence of loss thereby occasioned, is sufficient to discharge the surety. We find no difficulty whatever in answering this question in the negative. The rule of *strictissimi juris* is a stringent one, and is liable at times to work

> practical injustice. It is one which ought not to be extended to contracts not within the reason of the rule, particularly when the bond is underwritten by a corporation which has undertaken for a profit to insure the obligee against a failure or performance on the part of the principal obligor. Such a contract should be interpreted liberally in favor of the subcontractor, with a view of furthering the beneficent object of the statute. Of course, this rule would not extend to cases of fraud or unfair dealing on the part of the subcontractor, as was the case in United States use of Heise *v.* American Bonding & T. Co., 89 Fed. 921, 925, or to cases not otherwise within the scope of the undertaking."

It is respectfully submitted that in the case at bar the measure of liability sought to be imposed upon the surety is not within the scope of its undertaking.

The Supreme Court of Pennsylvania whose decisions have been quite generous toward the insured, nevertheless has said in

Young vs. American Bonding Company, 228 Pa 373 (1910),

in opinion by Mr. Justice Stewart:

> "In all essential particulars the Appellee here is an insurance company, and its obligation in this particular instance was that of an insurer. It was paid for its undertaking; the amount of its compensation being based on the calculation of risk assumed.
>
> It follows that there is but one way by which it is to be determined whether the variance complained of was a material variance. The test

is to be found in answer to the question, whether it substantially increased the chances of the loss insured against. If such were the result it would have been fair reason for demanding a higher premium than was paid and the materiality is thus made apparent. (Citations.) It is not a question whether the variance actually caused the breach of the bond; but whether it was such a variance as a reasonably careful and prudent person undertaking the risk would have regarded as substantially increasing the chances of loss."

Conclusion.

It is, therefore, respectfully submitted that this case is one calling for the exercise by your Honorable Court of its supervisory powers in order that this important question of general law may be settled and that to such an end a writ of certiorari should be granted and this Court should review the decision of the Circuit Court of Appeals and finally reverse it.

JAMES M. MAGEE,
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EDMUND W. ARTHUR,
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